

**Commission**

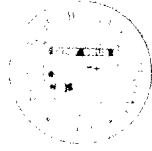
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**ARIZONA POWER AUTHORITY**

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October 31, 2005

Mr. Herbert R. Guenther  
AZ Department of Water Resources  
500 North Third Street  
Phoenix, AZ 85004

RE: Contribution for the Purpose of Defraying the Expense of Contracting  
With Outside Counsel for Colorado River Matters

Dear Mr. Guenther:

By letter dated September 15, 2005, Mr. Rick C. Lavis, Chairman of the Fundraising Committee for the Colorado River Legal Defense Fund requested a contribution from the Arizona Power Authority to support Arizona's legal position with respect to issues that can affect Arizona's allocation of Colorado River water. A.R.S. Section 30-104 of the Power Authority's enabling legislation provides for the Authority to cooperate with the Arizona Department of Water Resources in planning the hydroelectric power generation aspects of the development and use of the state's water resources. We believe this statutory direction sets state policy for joint cooperation between the Authority and the Department of Water Resources. However, cooperation is not unilateral and in order for it to exist, there must be reciprocity. We have been informed that certain representatives of the state's water interests have stated that power has no concern in this potential litigation.

The Arizona Power Authority represents electrical, irrigation, drainage and power districts and cities and towns throughout the state and we should have a voice in all activities undertaken by the Colorado River Defense Fund.

The Authority's primary responsibility is to bargain for, take and receive on behalf of the State of Arizona the electric power developed from the waters of the mainstream of the Colorado River. Hydroelectric power from Hoover Dam is extremely valuable to the State of Arizona and it is our responsibility to ensure that this resource is protected and used effectively and efficiently for the state and its people.

In order to properly appreciate the value of Hoover power it is helpful to compare the market value of Hoover power to the market value of Arizona's allocation of water from

the Colorado River. As you know the United States Supreme Court confirmed that Arizona is to receive 2.8 million acre feet of mainstream water from the Colorado River on an annual basis. If this water is valued at \$100.00 per acre-foot then the value of this resource to Arizona is \$280 million annually. Doing a similar calculation for the value of the Hoover power to the state is more complicated since the Hoover power can be evaluated from three perspectives, namely capacity, energy and pollution reduction. At today's market value for natural gas and using the capacity value established in the most recent contracts our customers entered into for the purchase of supplemental capacity, the Hoover power has a market value to the State of Arizona that is comparable to the value of the water that Arizona receives from the Colorado River. For this reason we believe the Hoover power should be given substantial consideration in the efforts undertaken by the Colorado River Legal Defense Fund.

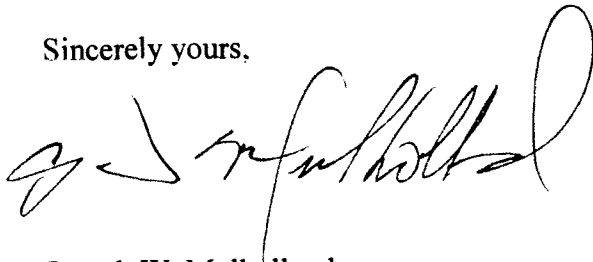
Essentially, the Arizona Power Authority believes that the various entities representing the interests of water and power users in this state should work together on a cooperative basis in defending the state's resources derived from the Colorado River.

With this principle in mind the Commission of the Arizona Power Authority unanimously adopted the following resolution at its October 18, 2005 Commission meeting:

The Arizona Power Authority will contribute, from the APA Fund, \$50,000.00 to the Colorado River Legal Defense Fund in equal installments over the next three years provided that the Power Authority is included in the discussions related to the proposed litigation and provided further that the value of the power generated from the mainstream of the Colorado River is protected by the efforts of the Colorado River Legal Defense Fund.

If the provisions of the Commission's Resolution are acceptable, please send me a note to that effect and the Authority will forward its first installment.

Sincerely yours,

A handwritten signature in black ink, appearing to read "J. W. Mulholland", written in a cursive style.

Joseph W. Mulholland  
Executive Director